
1 important to specifically quantify the benefits in a manner that the public can understand
2 and appreciate.

3 Q. IN YOUR OPINION, IS IT IN THE BEST INTERESTS OF PAWC'S CUSTOMERS FOR THE
4 COMMISSION TO GRANT A CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY TO THE
5 APPLICANTS THAT ALLOWS THAMES TO PURCHASE AWW?

6 A. In my opinion, it would be in the best interests of PAWC's customers for the
7 Commission to approve this transaction only if the Commission specifically adopts the
8 conditions summarized in Section VII of my testimony, and only if the Commission
9 requires PAWC to provide at least \$10 million in savings to its customers. If the
10 Commission fails to adopt the conditions that I recommend, and thereby fails to protect
11 consumers from the increased risks and other potential adverse effects of the acquisition,
12 then consumers would be better off if this transaction did not occur. Similarly, if the
13 Commission fails to require that significant savings are provided to consumers, such that
14 essentially all of the benefits from the acquisition flowed to the shareholders, officers,
15 and key employees of AWW, then PAWC's consumers would be better off if this
16 transaction did not occur.

17 Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

18 A. Yes, it does.

Appendix A

Scott J. Rubin

Attorney • Consultant

3 Lost Creek Drive • Selinsgrove, PA 17870

Current Position

Public Utility Attorney and Consultant, Selinsgrove, PA. 1994 to present. I provide legal, consulting, and expert witness services to various organizations interested in the regulation of public utilities.

Previous Positions

Lecturer in Computer Science, Susquehanna University, Selinsgrove, PA. 1993 to 2000.

Senior Assistant Consumer Advocate, Office of Consumer Advocate, Harrisburg, PA. 1990 to 1994.
I supervised the administrative and technical staff and shared with one other senior attorney the supervision of a legal staff of 14 attorneys.

Assistant Consumer Advocate, Office of Consumer Advocate, Harrisburg, PA. 1983 to 1990.

Associate, Laws and Staruch, Harrisburg, PA. 1981 to 1983.

Law Clerk, U.S. Environmental Protection Agency, Washington, DC. 1980 to 1981.

Research Assistant, Rockville Consulting Group, Washington, DC. 1979.

Current Professional Activities

Member, American Bar Association, Public Utility Law Section.

Member, American Water Works Association.

Admitted to practice law before the Supreme Court of Pennsylvania, the New York State Court of Appeals, the United States District Court for the Middle District of Pennsylvania, the United States Court of Appeals for the Third Circuit, and the Supreme Court of the United States.

Previous Professional Activities

Member, American Water Works Association, Rates and Charges Subcommittee, 1998-2001.

Member, Federal Advisory Committee on Disinfectants and Disinfection By-Products in Drinking Water, U.S. Environmental Protection Agency, Washington, DC. 1992 to 1994.

Chair, Water Committee, National Association of State Utility Consumer Advocates, Washington, DC. 1990 to 1994; member of committee from 1988 to 1990.

Member, Board of Directors, Pennsylvania Energy Development Authority, Harrisburg, PA. 1990 to 1994.

Member, Small Water Systems Advisory Committee, Pennsylvania Department of Environmental Resources, Harrisburg, PA. 1990 to 1992.

Member, Ad Hoc Committee on Emissions Control and Acid Rain Compliance, National Association of State Utility Consumer Advocates, 1991.

Member, Nitrogen Oxides Subcommittee of the Acid Rain Advisory Committee, U.S. Environmental Protection Agency, Washington DC. 1991.

Education

J.D. with Honors, George Washington University, Washington, DC. 1981.

B.A. with Distinction in Political Science, Pennsylvania State University, University Park, PA. 1978.

Publications and Presentations

“Quality of Service Issues,” a speech to the Pennsylvania Public Utility Commission Consumer Conference, State College, PA. 1988.

K.L. Pape and S.J. Rubin, “Current Developments in Water Utility Law,” in *Pennsylvania Public Utility Law* (Pennsylvania Bar Institute). 1990.

Presentation on Water Utility Holding Companies to the Annual Meeting of the National Association of State Utility Consumer Advocates, Orlando, FL. 1990.

“How the OCA Approaches Quality of Service Issues,” a speech to the Pennsylvania Chapter of the National Association of Water Companies. 1991.

Presentation on the Safe Drinking Water Act to the Mid-Year Meeting of the National Association of State Utility Consumer Advocates, Seattle, WA. 1991.

“A Consumer Advocate's View of Federal Pre-emption in Electric Utility Cases,” a speech to the Pennsylvania Public Utility Commission Electricity Conference. 1991.

Workshop on Safe Drinking Water Act Compliance Issues at the Mid-Year Meeting of the National Association of State Utility Consumer Advocates, Washington, DC. 1992.

Formal Discussant, Regional Acid Rain Workshop, U.S. Environmental Protection Agency and National Regulatory Research Institute, Charlotte, NC. 1992.

S.J. Rubin and S.P. O'Neal, “A Quantitative Assessment of the Viability of Small Water Systems in Pennsylvania,” *Proceedings of the Eighth NARUC Biennial Regulatory Information Conference*, National Regulatory Research Institute (Columbus, OH 1992), IV:79-97.

“The OCA's Concerns About Drinking Water,” a speech to the Pennsylvania Public Utility Commission Water Conference. 1992.

Member, Technical Horizons Panel, Annual Meeting of the National Association of Water Companies, Hilton Head, SC. 1992.

M.D. Klein and S.J. Rubin, “Water and Sewer -- Update on Clean Streams, Safe Drinking Water, Waste Disposal and Pennvest,” *Pennsylvania Public Utility Law Conference* (Pennsylvania Bar Institute). 1992.

Presentation on Small Water System Viability to the Technical Assistance Center for Small Water Companies, Pa. Department of Environmental Resources, Harrisburg, PA. 1993

- “The Results Through a Public Service Commission Lens,” speaker and participant in panel discussion at Symposium: “Impact of EPA’s Allowance Auction,” Washington, DC, sponsored by AER*X. 1993.
- “The Hottest Legislative Issue of Today -- Reauthorization of the Safe Drinking Water Act,” speaker and participant in panel discussion at the Annual Conference of the American Water Works Association, San Antonio, TX. 1993.
- “Water Service in the Year 2000,” a speech to the Conference: “Utilities and Public Policy III: The Challenges of Change,” sponsored by the Pennsylvania Public Utility Commission and the Pennsylvania State University, University Park, PA. 1993.
- “Government Regulation of the Drinking Water Supply: Is it Properly Focused?,” speaker and participant in panel discussion at the National Consumers League’s Forum on Drinking Water Safety and Quality, Washington, DC. 1993. Reprinted in *Rural Water*, Vol. 15 No. 1 (Spring 1994), pages 13-16.
- “Telephone Penetration Rates for Renters in Pennsylvania,” a study prepared for the Pennsylvania Office of Consumer Advocate. 1993.
- “Zealous Advocacy, Ethical Limitations and Considerations,” participant in panel discussion at “Continuing Legal Education in Ethics for Pennsylvania Lawyers,” sponsored by the Office of General Counsel, Commonwealth of Pennsylvania, State College, PA. 1993.
- “Serving the Customer,” participant in panel discussion at the Annual Conference of the National Association of Water Companies, Williamsburg, VA. 1993.
- “A Simple, Inexpensive, Quantitative Method to Assess the Viability of Small Water Systems,” a speech to the Water Supply Symposium, New York Section of the American Water Works Association, Syracuse, NY. 1993.
- S.J. Rubin, “Are Water Rates Becoming Unaffordable?,” *Journal American Water Works Association*, Vol. 86, No. 2 (February 1994), pages 79-86.
- “Why Water Rates Will Double (If We’re Lucky): Federal Drinking Water Policy and Its Effect on New England,” a briefing for the New England Conference of Public Utilities Commissioners, Andover, MA. 1994.
- “Are Water Rates Becoming Unaffordable?,” a speech to the Legislative and Regulatory Conference, Association of Metropolitan Water Agencies, Washington, DC. 1994.
- “Relationships: Drinking Water, Health, Risk and Affordability,” speaker and participant in panel discussion at the Annual Meeting of the Southeastern Association of Regulatory Commissioners, Charleston, SC. 1994.
- “Small System Viability: Assessment Methods and Implementation Issues,” speaker and participant in panel discussion at the Annual Conference of the American Water Works Association, New York, NY. 1994.

- S.J. Rubin, "How much should we spend to save a life?," *Seattle Journal of Commerce*, August 18, 1994 (Protecting the Environment Supplement), pages B-4 to B-5.
- S. Rubin, S. Bernow, M. Fulmer, J. Goldstein, and I. Peters, *An Evaluation of Kentucky-American Water Company's Long-Range Planning*, prepared for the Utility and Rate Intervention Division, Kentucky Office of the Attorney General (Tellus Institute 1994).
- S.J. Rubin, "Small System Monitoring: What Does It Mean?," *Impacts of Monitoring for Phase II/V Drinking Water Regulations on Rural and Small Communities* (National Rural Water Association 1994), pages 6-12.
- "Surviving the Safe Drinking Water Act," speaker at the Annual Meeting of the National Association of State Utility Consumer Advocates, Reno, NV. 1994.
- "Safe Drinking Water Act Compliance -- Ratemaking Implications," speaker at the National Conference of Regulatory Attorneys, Scottsdale, AZ. 1995. Reprinted in *Water*, Vol. 36, No. 2 (Summer 1995), pages 28-29.
- S.J. Rubin, "Water: Why Isn't it Free? The Case of Small Utilities in Pennsylvania," *Utilities, Consumers & Public Policy: Issues of Quality, Affordability, and Competition, Proceedings of the Fourth Utilities, Consumers and Public Policy Conference* (Pennsylvania State University 1995), pages 177-183.
- S.J. Rubin, "Water Rates: An Affordable Housing Issue?," *Home Energy*, Vol. 12 No. 4 (July/August 1995), page 37.
- Speaker and participant in the Water Policy Forum, sponsored by the National Association of Water Companies, Naples, FL. 1995.
- Participant in panel discussion on "The Efficient and Effective Maintenance and Delivery of Potable Water at Affordable Rates to the People of New Jersey," at The New Advocacy: Protecting Consumers in the Emerging Era of Utility Competition, a conference sponsored by the New Jersey Division of the Ratepayer Advocate, Newark, NJ. 1995.
- J.E. Cromwell III, and S.J. Rubin, *Development of Benchmark Measures for Viability Assessment* (Pa. Department of Environmental Protection 1995).
- S. Rubin, "A Nationwide Practice from a Small Town in Pa.," *Lawyers & the Internet - a Supplement to the Legal Intelligencer and Pa. Law Weekly* (February 12, 1996), page S6.
- "Changing Customers' Expectations in the Water Industry," speaker at the Mid-America Regulatory Commissioners Conference, Chicago, IL. 1996, reprinted in *Water* Vol. 37 No. 3 (Winter 1997), pages 12-14..
- "Recent Federal Legislation Affecting Drinking Water Utilities," speaker at Pennsylvania Public Utility Law Conference, Pennsylvania Bar Institute, Hershey, PA. 1996.
- "Clean Water at Affordable Rates: A Ratepayers Conference," moderator at symposium sponsored by the New Jersey Division of Ratepayer Advocate, Trenton, NJ. 1996.

- “Water Workshop: How New Laws Will Affect the Economic Regulation of the Water Industry,” speaker at the Annual Meeting of the National Association of State Utility Consumer Advocates, San Francisco, CA. 1996.
- E.T. Castillo, S.J. Rubin, S.K. Keefe, and R.S. Raucher, “Restructuring Small Systems,” *Journal American Water Works Association*, Vol. 89, No. 1 (January 1997), pages 65-74.
- J.E. Cromwell III, S.J. Rubin, F.C. Marrocco, and M.E. Leevan, “Business Planning for Small System Capacity Development,” *Journal American Water Works Association*, Vol. 89, No. 1 (January 1997), pages 47-57.
- “Capacity Development – More than Viability Under a New Name,” speaker at National Association of Regulatory Utility Commissioners Winter Meetings, Washington, DC. 1997.
- E. Castillo, S.K. Keefe, R.S. Raucher, and S.J. Rubin, *Small System Restructuring to Facilitate SDWA Compliance: An Analysis of Potential Feasibility* (AWWA Research Foundation, 1997).
- H. Himmelberger, *et al.*, *Capacity Development Strategy Report for the Texas Natural Resource Conservation Commission* (Aug. 1997).
- Briefing on Issues Affecting the Water Utility Industry, Annual Meeting of the National Association of State Utility Consumer Advocates, Boston, MA. 1997.
- “Capacity Development in the Water Industry,” speaker at the Annual Meeting of the National Association of Regulatory Utility Commissioners, Boston, MA. 1997.
- “The Ticking Bomb: Competitive Electric Metering, Billing, and Collection,” speaker at the Annual Meeting of the National Association of State Utility Consumer Advocates, Boston, MA. 1997.
- Scott J. Rubin, “A Nationwide Look at the Affordability of Water Service,” *Proceedings of the 1998 Annual Conference of the American Water Works Association*, Water Research, Vol. C, No. 3, pages 113-129 (American Water Works Association, 1998).
- Scott J. Rubin, “30 Technology Tips in 30 Minutes,” *Pennsylvania Public Utility Law Conference*, Vol. I, pages 101-110 (Pa. Bar Institute, 1998).
- Scott J. Rubin, “Effects of Electric and Gas Deregulation on the Water Industry,” *Pennsylvania Public Utility Law Conference*, Vol. I, pages 139-146 (Pa. Bar Institute, 1998).
- Scott J. Rubin, *The Challenges and Changing Mission of Utility Consumer Advocates* (American Association of Retired Persons, 1999).
- “Consumer Advocacy for the Future,” speaker at the Age of Awareness Conference, Changes and Choices: Utilities in the New Millennium, Carlisle, PA. 1999.
- Keynote Address, \$1 Energy Fund, Inc., Annual Membership Meeting, Monroeville, PA. 1999.

- Scott J. Rubin, "Assessing the Effect of the Proposed Radon Rule on the Affordability of Water Service," prepared for the American Water Works Association. 1999.
- Scott J. Rubin and Janice A. Beecher, The Impacts of Electric Restructuring on the Water and Wastewater Industry, *Proceedings of the Small Drinking Water and Wastewater Systems International Symposium and Technology Expo* (Phoenix, AZ 2000), pp. 66-75.
- American Water Works Association, *Principles of Water Rates, Fees, and Charges, Manual M1 – Fifth Edition* (AWWA 2000), Member, Editorial Committee.
- Janice A. Beecher and Scott J. Rubin, presentation on "Special Topics in Rate Design: Affordability" at the Annual Conference and Exhibition of the American Water Works Association, Denver, CO. 2000.
- Scott J. Rubin, "The Future of Drinking Water Regulation," a speech at the Annual Conference and Exhibition of the American Water Works Association, Denver, CO. 2000.
- Janice A. Beecher and Scott J. Rubin, "Deregulation Impacts and Opportunities," a presentation at the Annual Conference and Exhibition of the American Water Works Association, Denver, CO. 2000.
- Scott J. Rubin, "Estimating the Effect of Different Arsenic Maximum Contaminant Levels on the Affordability of Water Service," prepared for the American Water Works Association. 2000.
- Janice A. Beecher and Scott J. Rubin, *Deregulation! Impacts on the Water Industry*, American Water Works Association Research Foundation, Denver, CO. 2000.
- Scott J. Rubin, Methods for Assessing, Evaluating, and Assisting Small Water Systems, NARUC Annual Regulatory Studies Program, East Lansing, MI. 2000.
- Scott J. Rubin, Consumer Issues in the Water Industry, NARUC Annual Regulatory Studies Program, East Lansing, MI. 2000.
- "Be Utility Wise in a Restructured Utility Industry," Keynote Address at Be UtilityWise Conference, Pittsburgh, PA. 2000.
- Scott J. Rubin, Jason D. Sharp, and Todd S. Stewart, "The Wired Administrative Lawyer," *5th Annual Administrative Law Symposium*, Pennsylvania Bar Institute, Harrisburg, PA. 2000.
- Scott J. Rubin, "Current Developments in the Water Industry," *Pennsylvania Public Utility Law Conference*, Pennsylvania Bar Institute, Harrisburg, PA. 2000.
- Scott J. Rubin, "Viewpoint: Change Sickening Attitudes," *Engineering News-Record*, Dec. 18, 2000.
- Janice A. Beecher and Scott J. Rubin, "Ten Practices of Highly Effective Water Utilities," *Opflow*, April 2001, pp. 1, 6-7, 16.
- Scott J. Rubin, "Pennsylvania Utilities: How Are Consumers, Workers, and Corporations Faring in the Deregulated Electricity, Gas, and Telephone Industries?" Keystone Research Center, May 2001.

Scott J. Rubin, "Guest Perspective: A First Look at the Impact of Electric Deregulation on Pennsylvania," *LEAP Letter*, May-June 2001, pp. 2-3.

Testimony as an Expert Witness

Pa. Public Utility Commission v. Pennsylvania Gas and Water Co. - Water Division, Pa. Public Utility Commission, Docket R-00922404. 1992. Concerning rate design, on behalf of the Pa. Office of Consumer Advocate.

Pa. Public Utility Commission v. Shenango Valley Water Co., Pa. Public Utility Commission, Docket R-00922420. 1992. Concerning cost allocation, on behalf of the Pa. Office of Consumer Advocate

Pa. Public Utility Commission v. Pennsylvania Gas and Water Co. - Water Division, Pa. Public Utility Commission, Docket R-00922482. 1993. Concerning rate design, on behalf of the Pa. Office of Consumer Advocate

Pa. Public Utility Commission v. Colony Water Co., Pa. Public Utility Commission, Docket R-00922375. 1993. Concerning rate design, on behalf of the Pa. Office of Consumer Advocate

Pa. Public Utility Commission v. Dauphin Consolidated Water Supply Co. and General Waterworks of Pennsylvania, Inc., Pa. Public Utility Commission, Docket R-00932604. 1993. Concerning rate design and cost of service, on behalf of the Pa. Office of Consumer Advocate

West Penn Power Co. v. State Tax Department of West Virginia, Circuit Court of Kanawha County, West Virginia, Civil Action No. 89-C-3056. 1993. Concerning regulatory policy and the effects of a taxation statute on out-of-state utility ratepayers, on behalf of the Pa. Office of Consumer Advocate

Pa. Public Utility Commission v. Pennsylvania Gas and Water Co. - Water Division, Pa. Public Utility Commission, Docket R-00932667. 1993. Concerning rate design and affordability of service, on behalf of the Pa. Office of Consumer Advocate

Pa. Public Utility Commission v. National Utilities, Inc., Pa. Public Utility Commission, Docket R-00932828. 1994. Concerning rate design, on behalf of the Pa. Office of Consumer Advocate

An Investigation of the Sources of Supply and Future Demand of Kentucky-American Water Company, Ky. Public Service Commission, Case No. 93-434. 1994. Concerning supply and demand planning, on behalf of the Kentucky Office of Attorney General, Utility and Rate Intervention Division.

The Petition on Behalf of Gordon's Corner Water Company for an Increase in Rates, New Jersey Board of Public Utilities, Docket No. WR94020037. 1994. Concerning revenue requirements and rate design, on behalf of the New Jersey Division of Ratepayer Advocate.

Re Consumers Maine Water Company Request for Approval of Contracts with Consumers Water Company and with Ohio Water Service Company, Me. Public Utilities Commission, Docket No. 94-352. 1994. Concerning affiliated interest agreements, on behalf of the Maine Public Advocate.

In the Matter of the Application of Potomac Electric Power Company for Approval of its Third Least-Cost Plan, D.C. Public Service Commission, Formal Case No. 917, Phase II. 1995. Concerning Clean Air Act implementation and environmental externalities, on behalf of the District of Columbia Office of the People's Counsel.

- In the Matter of the Regulation of the Electric Fuel Component Contained within the Rate Schedules of the Dayton Power and Light Company and Related Matters*, Ohio Public Utilities Commission, Case No. 94-105-EL-EFC. 1995. Concerning Clean Air Act implementation (case settled before testimony was filed), on behalf of the Office of the Ohio Consumers' Counsel.
- Kennebec Water District Proposed Increase in Rates*, Maine Public Utilities Commission, Docket No. 95-091. 1995. Concerning the reasonableness of planning decisions and the relationship between a publicly owned water district and a very large industrial customer, on behalf of the Maine Public Advocate.
- Winter Harbor Water Company, Proposed Schedule Revisions to Introduce a Readiness-to-Serve Charge*, Maine Public Utilities Commission, Docket No. 95-271. 1995 and 1996. Concerning standards for, and the reasonableness of, imposing a readiness to serve charge and/or exit fee on the customers of a small investor-owned water utility, on behalf of the Maine Public Advocate.
- In the Matter of the 1995 Long-Term Electric Forecast Report of the Cincinnati Gas & Electric Company*, Public Utilities Commission of Ohio, Case No. 95-203-EL-FOR, and *In the Matter of the Two-Year Review of the Cincinnati Gas & Electric Company's Environmental Compliance Plan Pursuant to Section 4913.05, Revised Cost*, Case No. 95-747-EL-ECP. 1996. Concerning the reasonableness of the utility's long-range supply and demand-management plans, the reasonableness of its plan for complying with the Clean Air Act Amendments of 1990, and discussing methods to ensure the provision of utility service to low-income customers, on behalf of the Office of the Ohio Consumers' Counsel.
- In the Matter of Notice of the Adjustment of the Rates of Kentucky-American Water Company*, Kentucky Public Service Commission, Case No. 95-554. 1996. Concerning rate design, cost of service, and sales forecast issues, on behalf of the Kentucky Office of Attorney General.
- In the Matter of the Application of Citizens Utilities Company for a Hearing to Determine the Fair Value of its Properties for Ratemaking Purposes, to Fix a Just and Reasonable Rate of Return Thereon, and to Approve Rate Schedules Designed to Provide such Rate of Return*, Arizona Corporation Commission, Docket Nos. E-1032-95-417, et al. 1996. Concerning rate design, cost of service, and the price elasticity of water demand, on behalf of the Arizona Residential Utility Consumer Office.
- Cochrane v. Bangor Hydro-Electric Company*, Maine Public Utilities Commission, Docket No. 96-053. 1996. Concerning regulatory requirements for an electric utility to engage in unregulated business enterprises, on behalf of the Maine Public Advocate.
- In the Matter of the Regulation of the Electric Fuel Component Contained within the Rate Schedules of Monongahela Power Company and Related Matters*, Public Utilities Commission of Ohio, Case No. 96-106-EL-EFC. 1996. Concerning the costs and procedures associated with the implementation of the Clean Air Act Amendments of 1990, on behalf of the Ohio Consumers' Counsel.
- In the Matter of the Regulation of the Electric Fuel Component Contained within the Rate Schedules of Cleveland Electric Illuminating Company and Toledo Edison Company and Related Matters*, Public Utilities Commission of Ohio, Case Nos. 96-107-EL-EFC and 96-108-EL-EFC. 1996.

Concerning the costs and procedures associated with the implementation of the Clean Air Act Amendments of 1990, on behalf of the Ohio Consumers' Counsel.

In the Matter of the Regulation of the Electric Fuel Component Contained within the Rate Schedules of Ohio Power Company and Columbus Southern Power Company and Related Matters, Public Utilities Commission of Ohio, Case Nos. 96-101-EL-EFC and 96-102-EL-EFC. 1997. Concerning the costs and procedures associated with the implementation of the Clean Air Act Amendments of 1990, on behalf of the Ohio Consumers' Counsel.

An Investigation of the Sources of Supply and Future Demand of Kentucky-American Water Company (Phase II), Kentucky Public Service Commission, Docket No. 93-434. 1997. Concerning supply and demand planning, on behalf of the Kentucky Office of Attorney General, Public Service Litigation Branch.

In the Matter of the Regulation of the Electric Fuel Component Contained within the Rate Schedules of Cincinnati Gas and Electric Co. and Related Matters, Public Utilities Commission of Ohio, Case No. 96-103-EL-EFC. 1997. Concerning the costs and procedures associated with the implementation of the Clean Air Act Amendments of 1990, on behalf of the Ohio Consumers' Counsel.

Bangor Hydro-Electric Company Petition for Temporary Rate Increase, Maine Public Utilities Commission, Docket No. 97-201. 1997. Concerning the reasonableness of granting an electric utility's request for emergency rate relief, and related issues, on behalf of the Maine Public Advocate.

Testimony concerning H.B. 1068 Relating to Restructuring of the Natural Gas Utility Industry, Consumer Affairs Committee, Pennsylvania House of Representatives. 1997. Concerning the provisions of proposed legislation to restructure the natural gas utility industry in Pennsylvania, on behalf of the Pennsylvania AFL-CIO Gas Utility Caucus.

In the Matter of the Regulation of the Electric Fuel Component Contained within the Rate Schedules of Cleveland Electric Illuminating Company and Toledo Edison Company and Related Matters, Public Utilities Commission of Ohio, Case Nos. 97-107-EL-EFC and 97-108-EL-EFC. 1997. Concerning the costs and procedures associated with the implementation of the Clean Air Act Amendments of 1990, on behalf of the Ohio Consumers' Counsel.

In the Matter of the Petition of Valley Road Sewerage Company for a Revision in Rates and Charges for Water Service, New Jersey Board of Public Utilities, Docket No. WR92080846J. 1997. Concerning the revenue requirements and rate design for a wastewater treatment utility, on behalf of the New Jersey Division of Ratepayer Advocate.

Bangor Gas Company, L.L.C., Petition for Approval to Furnish Gas Service in the State of Maine, Maine Public Utilities Commission, Docket No. 97-795. 1998. Concerning the standards and public policy concerns involved in issuing a certificate of public convenience and necessity for a new natural gas utility, and related ratemaking issues, on behalf of the Maine Public Advocate.

In the Matter of the Investigation on Motion of the Commission into the Adequacy of the Public Utility Water Service Provided by Tidewater Utilities, Inc., in Areas in Southern New Castle County, Delaware, Delaware Public Service Commission, Docket No. 309-97. 1998. Concerning the

standards for the provision of efficient, sufficient, and adequate water service, and the application of those standards to a water utility, on behalf of the Delaware Division of the Public Advocate.

In the Matter of the Regulation of the Electric Fuel Component Contained within the Rate Schedules of Cincinnati Gas and Electric Co. and Related Matters, Public Utilities Commission of Ohio, Case No. 97-103-EL-EFC. 1998. Concerning fuel-related transactions with affiliated companies and the appropriate ratemaking treatment and regulatory safeguards involving such transactions, on behalf of the Ohio Consumers' Counsel.

Olde Port Mariner Fleet, Inc. Complaint Regarding Casco Bay Island Transit District's Tour and Charter Service, Maine Public Utilities Commission, Docket No. 98-161. 1998. Concerning the standards and requirements for allocating costs and separating operations between regulated and unregulated operations of a transportation utility, on behalf of the Maine Public Advocate and Olde Port Mariner Fleet, Inc.

Central Maine Power Company Investigation of Stranded Costs, Transmission and Distribution Utility Revenue Requirements, and Rate Design, Maine Public Utilities Commission, Docket No. 97-580. 1998. Concerning the treatment of existing rate discounts when designing rates for a transmission and distribution electric utility, on behalf of the Maine Public Advocate.

Pa. Public Utility Commission v. Manufacturers Water Company, Pennsylvania Public Utility Commission, Docket No. R-00984275. 1998. Concerning rate design on behalf of the Manufacturers Water Industrial Users.

In the Matter of Petition of Pennsgrove Water Supply Company for an Increase in Rates for Water Service, New Jersey Board of Public Utilities, Docket No. WR98030147. 1998. Concerning the revenue requirements, level of affiliated charges, and rate design for a water utility, on behalf of the New Jersey Division of Ratepayer Advocate.

In the Matter of Petition of Seaview Water Company for an Increase in Rates for Water Service, New Jersey Board of Public Utilities, Docket No. WR98040193. 1999. Concerning the revenue requirements and rate design for a water utility, on behalf of the New Jersey Division of Ratepayer Advocate.

In the Matter of the Regulation of the Electric Fuel Component Contained within the Rate Schedules of Ohio Power Company and Columbus Southern Power Company and Related Matters, Public Utilities Commission of Ohio, Case Nos. 98-101-EL-EFC and 98-102-EL-EFC. 1999. Concerning the costs and procedures associated with the implementation of the Clean Air Act Amendments of 1990, on behalf of the Ohio Consumers' Counsel.

In the Matter of the Regulation of the Electric Fuel Component Contained within the Rate Schedules of Dayton Power and Light Company and Related Matters, Public Utilities Commission of Ohio, Case No. 98-105-EL-EFC. 1999. Concerning the costs and procedures associated with the implementation of the Clean Air Act Amendments of 1990, on behalf of the Ohio Consumers' Counsel.

In the Matter of the Regulation of the Electric Fuel Component Contained within the Rate Schedules of Monongahela Power Company and Related Matters, Public Utilities Commission of Ohio, Case No. 99-106-EL-EFC. 1999. Concerning the costs and procedures associated with the

implementation of the Clean Air Act Amendments of 1990, on behalf of the Ohio Consumers' Counsel.

County of Suffolk, et al. v. Long Island Lighting Company, et al., U.S. District Court for the Eastern District of New York, Case No. 87-CV-0646. 2000. Submitted two affidavits concerning the calculation and collection of court-ordered refunds to utility customers, on behalf of counsel for the plaintiffs.

Northern Utilities, Inc., Petition for Waivers from Chapter 820, Maine Public Utilities Commission, Docket No. 99-254. 2000. Concerning the standards and requirements for defining and separating a natural gas utility's core and non-core business functions, on behalf of the Maine Public Advocate.

Notice of Adjustment of the Rates of Kentucky-American Water Company, Kentucky Public Service Commission, Case No. 2000-120. 2000. Concerning the appropriate methods for allocating costs and designing rates, on behalf of the Kentucky Office of Attorney General.

In the Matter of the Petition of Gordon's Corner Water Company for an Increase in Rates and Charges for Water Service, New Jersey Board of Public Utilities, Docket No. WR00050304. 2000. Concerning the revenue requirements and rate design for a water utility, on behalf of the New Jersey Division of Ratepayer Advocate.

Testimony concerning Arsenic in Drinking Water: An Update on the Science, Benefits, and Costs, Committee on Science, United States House of Representatives. 2001. Concerning the effects on low-income households and small communities from a more stringent regulation of arsenic in drinking water.

In the Matter of the Application of The Cincinnati Gas & Electric Company for an Increase in Gas Rates in its Service Territory, Public Utilities Commission of Ohio, Case No. 01-1228-GA-AIR, et al. 2002. Concerning the need for and structure of a special rider and alternative form of regulation for an accelerated main replacement program, on behalf of the Ohio Consumers' Counsel.

Pennsylvania State Treasurer's Hearing on Enron and Corporate Governance Issues. 2002. Concerning Enron's role in Pennsylvania's electricity market and related issues, on behalf of the Pennsylvania AFL-CIO.

An Investigation into the Feasibility and Advisability of Kentucky-American Water Company's Proposed Solution to its Water Supply Deficit, Kentucky Public Service Commission, Case No. 2001-00117. 2002. Concerning water supply planning, regulatory oversight, and related issue, on behalf of the Kentucky Office of Attorney General.

I/M/O the Joint Petition of New Jersey-American Water Company, Inc. and
Thames Water Aqua Holdings GmbH for Approval of Change in Control
of New Jersey-American Water Company, Inc.
BPU Docket No. WM01120833

REQUEST OCE-3
Page 1 of 1

Q. Discuss how RWE/Thames would unwind the transaction in the event that it did not meet financial and/or growth expectations of the parent company. How will RWE measure whether the acquisition has been successful? Discuss how RWE will allocate capital among its various operations worldwide. Explain how a change in the investment climate in Europe versus the United States would influence the capital allocation process. Discuss the effect of the acquisition on the free cash flow of RWE. Would RWE consider selling parts of its United States' acquisitions to other parties? Explain.

A. The financial and growth targets of the business are as identified in the investment advisor reports referenced in response to request OCE-1. RWE is confident that these targets will be achieved and will support the Americas management in achievement of these goals. Because it is not anticipated that the financial and growth targets will not be met, RWE and Thames have not analyzed how the transaction would be unwound.

RWE will allocate capital among its various operations worldwide in order to meet the obligations imposed on such subsidiaries, including in the case of NJAWC, the regulatory and service obligations of NJAWC. By acquiring NJAWC, RWE undertakes the legal responsibility to provide safe and reliable service pursuant to applicable statutes. RWE/NJAWC will undertake the capital investments necessary to satisfy these obligations, assuming that the Board continues to provide NJAWC with a opportunity to achieve a reasonable return on investment. It is anticipated that the proposed transaction will generate positive cash flows.

A change in the investment climate in Europe versus the United States would influence the capital allocation process only to the extent that RWE has discretionary investment opportunities.

RWE is committed to growing its four core utility divisions. Therefore, there are no current plans to divest any of the water division acquisitions in the US. As publicly stated non-core assets such as Turner Construction and Heidleberg Press are being considered for disposal.

**American Water Works Corp.
Customers in States Where Merger is Contested (including Citizens)**

State	Customers	% of Total
AZ	84,000	4.5%
CA	176,000	9.4%
IL	255,000	13.6%
KY	102,000	5.5%
MD	5,000	0.3%
NJ	346,000	18.5%
NM	14,000	0.7%
NY	74,000	4.0%
PA	606,000	32.4%
VA	53,000	2.8%
WV	<u>156,000</u>	8.3%
Total	1,871,000	

Notes:

AZ Appl. para. 1 - 5,000 customers; plus 79,000 from Citizens (145,000 for AZ+CA per AWW3/28/02 10K; 66,000 in CA per Kelleher CA testimony Q.8)

CA Petition para. 12; Kelleher test. Q.8

IL Gloriod test. pp. 5-6

KY Mundy test. pp. 4-5

MD Petition para. 1

NJ http://www.amwater.com/awpr/njaw/about_us/aboutus.html

NM Stephenson test. p. 5

NY Petition para. 1

PA AWW 3/28/02 10K, Exh. 13, p. 7

VA As of 12/31/00 per AWW 2000 annual report

WV Petition para. 2

**PENNSYLVANIA
PUBLIC UTILITY COMMISSION
Harrisburg, PA 17105-3265**

Public Meeting held August 29, 2002

Commissioners Present:

Glen R. Thomas, Chairman,
Robert K. Bloom, Vice Chairman
Aaron Wilson, Jr.
Terrance J. Fitzpatrick
Kim Pizzingrilli

Joint Application of Pennsylvania-American
Water Company and Thames Water Aqua
Holdings GmbH for all approvals required under
the Public Utility Code in connection with a
change in control of Pennsylvania-American
Water Company

A-212285F0096
A-230073F0004

OPINION AND ORDER

BY THE COMMISSION:

Before the Commission for consideration and disposition are the Exceptions filed separately on July 11, 2002, by the following Parties: the Office of Consumer Advocate (OCA); the Office of Trial Staff (OTS); and the Citizens for Pennsylvania's Future, d/b/a Penn Future, Defend Our Watershed!, Daniel S. Townsend, and Joseph Laver (collectively, the PennFuture Parties). These Exceptions were filed regarding the Initial Decision of Administrative Law Judge (ALJ) Wayne L. Weismandel issued on June 21, 2002, in the above-captioned proceeding. Replies to the Exceptions were filed on July 22, 2002, by the Pennsylvania-American Water Company (PAWC) and Thames Water Aqua Holdings GmbH (Thames) (collectively, Joint Applicants).

History of the Proceeding¹

On December 14, 2001, the Joint Applicants filed a Joint Application for all approvals required under the Public Utility Code in connection with a change in control of Pennsylvania-American Water Company (Joint Application). Timely Protests or Notices to Intervene were filed by the following Parties: Utility Workers Union of America, AFL-CIO (UWUA) and the Utility Workers Union of America Local Union No. 537 (Local 537) (Union Protest); the OCA; the OTS; and the Office of Small Business Advocate (OSBA).

On March 1, 2002, the PennFuture Parties filed a late-filed Petition to Intervene and Protest. This Petition was granted by Order dated March 12, 2002.

On March 5, 2002, UWUA and Local 537 filed a letter dated the same date stating that they had “reached a settlement” resolving their concerns with respect to the proposed acquisition of PAWC by Thames. On March 15, 2002, UWUA filed a Memorandum of Agreement between UWUA and Thames dated March 1, 2002.

On March 18, 2002, the Commission on Economic Opportunity (CEO) filed a late-filed Petition to Intervene (CEO Petition). On April 10, 2002, Joint Applicants timely filed their Answer in Opposition (CEO Petition Answer) to the CEO Petition. By Initial Decision dated April 11, 2002 (April 11th Initial Decision), the ALJ denied the CEO Petition.

Public Input Hearings were held in two sessions (1:00 p.m. and 6:30 p.m.) on April 24, 2002, at King’s College, Wilkes-Barre, Pennsylvania. Representatives on

behalf of all active participants attended. A total of twenty-four witnesses (including Representatives Phyllis Mundy and John Yudichak) presented sworn testimony at the two sessions of the Public Input Hearing. A transcript of the 1:00 p.m. session containing 66 pages (numbered 18 through 83) and a transcript of the 6:30 p.m. session containing 61 pages (numbered 84 through 144) were prepared.

On April 25, 2002, CEO filed Exceptions (CEO Exceptions) to the April 11th Initial Decision, a Motion for Stay of Proceedings (CEO Stay Motion), and a copy of a Petition for Review filed with the Commonwealth Court of Pennsylvania. (*See* No. 1037 C.D. 2002). On May 2, 2002, OCA filed Exceptions (OCA Exceptions) to the April 11th Initial Decision. On May 6, 2002, Joint Applicants filed their Answer (Stay Motion Answer) to the CEO Stay Motion. By Opinion and Order entered on May 9, 2002, the Commission denied the CEO Stay Motion, the CEO Exceptions, and the OCA Exceptions.

The Initial Hearing convened as scheduled on May 7, 2002. Representatives of Joint Applicants, the OCA, the OTS, the PennFuture Parties, and the OSBA participated. A transcript of the Initial Hearing containing 183 pages was produced. All active participants completed presentation of their evidence on May 7, 2002. Timely Main Briefs were filed by Joint Applicants, the OCA, the OTS, and the PennFuture Parties. Timely Reply Briefs were filed by Joint Applicants, the OCA, and the PennFuture Parties.

In the Initial Decision, the ALJ recommended that we find that the Applicants have met their burden of proof and that the Application be granted, subject to certain conditions which the Joint Applicants agreed to accept. As mentioned above,

¹ Portions of this Section are adopted from pages 1-8 of the Initial Decision

timely Exceptions were filed by the OCA, the OTS, and the PennFuture Parties. The Joint Applicants filed timely Replies to the Exceptions.

Discussion

The ALJ made specific Findings of Fact and Conclusions of Law (I.D., pp. 8-15 and 37-40, respectively), which are adopted herein by reference, unless modified or reversed, expressly or by necessary implication, by this Opinion and Order.

A. Description of the Companies and the Proposed Merger

The ALJ described, at pages 15-18 of the Initial Decision, the Parties and circumstances surrounding this Joint Merger Application. On September 16, 2001, American Water Works Company, Inc. (AWWC), the parent of PAWC, entered into an Agreement and Plan of Merger (Merger Agreement) with RWE Aktiengesellschaft (RWE), Thames, a wholly-owned subsidiary of RWE, and Apollo Acquisition Company (Apollo), a subsidiary of Thames. Pursuant to the terms of the Merger Agreement, AWWC and Apollo would merge and AWWC, the surviving corporation, would become a wholly-owned direct or indirect subsidiary of Thames. On December 14, 2001, the Joint Applicants filed their Joint Application in pursuance of the Merger Agreement. The parties, the transaction and the approvals requested by the Joint Applicants are more fully described below.

PAWC is a Pennsylvania corporation that provides regulated water and wastewater service. As of year-end 2001, PAWC furnished water service to approximately 568,000 customers and wastewater service to approximately 11,000 customers.

without further attribution.

With PAWC's acquisition of the assets and service areas of Citizens Utilities Water Company of Pennsylvania, in January 2002, and Lehman Pike Water and Sewer Company, in April 2002, PAWC currently provides service to 604,000 water and 12,500 wastewater customers. PAWC's service territory covers 35 counties and encompasses 357 municipalities with a total population served of approximately 2 million. PAWC is a wholly-owned subsidiary of AWWC.

AWWC is a Delaware corporation that owns the stock of various subsidiary operating water and wastewater utilities, including PAWC. AWWC also owns the stock of non-utility subsidiaries including the American Water Works Service Company, which provides a variety of services to AWWC's operating utilities; the American Water Capital Corporation, which is the financing vehicle for the AWWC system; and other subsidiaries that are in the business of providing management services to water and wastewater systems owned by others. Through its operating water and wastewater companies, AWWC furnishes service to approximately 15 million consumers throughout the United States and Canada. AWWC is the largest investor-owned water utility holding company in the United States. AWWC is a public company, and its stock is listed and actively traded on the New York Stock Exchange.

Thames is a company organized under the laws of the Federal Republic of Germany. Thames owns several subsidiaries including Thames Water Plc (Thames Water), which is the management company responsible for the operations of all of Thames' water and wastewater businesses (collectively, Thames and Thames Water will be referred to as Thames Germany).

Thames Germany is the largest water/wastewater utility in the United Kingdom, where it provides service to 12 million people in and around the City of

London, and the third largest water/wastewater services company in the world, serving over 43 million people world-wide. Within the United States, Thames Germany owns E'town Corporation (E'town), one of the nation's largest investor-owned water and wastewater utilities. Through its subsidiaries, Elizabethtown Water Company, Mount Holly Water Company and Applied Wastewater Management, Inc., E'town provides water and wastewater service to approximately one million people in 54 municipalities located throughout eight counties in central New Jersey. E'town also provides water and wastewater management services in New Jersey through two non-regulated subsidiaries. A detailed corporate profile of Thames Germany is set forth in Exhibit C to the Joint Application.

RWE, the parent of Thames, is a company organized under the laws of the Federal Republic of Germany. RWE is a leading international multi-utility company with core businesses in electricity, water, natural gas and waste management. RWE is the largest electric company in Germany and the third largest electricity provider in Europe. With its Thames Germany subsidiaries, RWE is the third largest water supplier in the world. RWE is also the second largest natural gas supplier in Germany. In addition, RWE has a leading position in the global coal market through Pittsburgh-based CONSOL Energy Inc., which is the second largest coal producer in the United States and the sixth largest world-wide. RWE has a total market capitalization in excess of \$21 billion, which would rank it second only to Duke Energy among domestic electric, gas and water utilities. A detailed corporate profile of RWE is set forth in Exhibit B to the Joint Application.

Apollo is a Delaware corporation formed solely for the purpose of merging into AWWC and has not conducted any unrelated activities since its organization. Apollo is a wholly-owned subsidiary of Thames.

The merger of AWWC with Apollo will result in AWWC becoming a wholly-owned subsidiary of Thames. PAWC will continue to be a subsidiary of AWWC. In short, the merger will affect only the ownership of the shares of AWWC. The corporate identities, corporate structures and assets of AWWC and PAWC will be unaffected, and PAWC will continue to exist as a Pennsylvania corporation subject to the jurisdiction and regulation of the Commission. A complete copy of the Merger Agreement was provided as Exhibit A to the Joint Application. Organizational charts depicting the present corporate structure of AWWC and RWE, the structural elements of the proposed transaction and the post-merger corporate alignment are provided in Attachment 2 to Joint Applicants' Statement 2.

Under the terms of the Merger Agreement, outstanding shares of AWWC's common stock not already owned by Thames or its affiliates will be converted into a right to receive payment of \$46.00 per share, unless the holder exercises the appraisal rights granted under Delaware law. The Merger Agreement further provides that AWWC's outstanding non-debt senior securities, consisting of Preferred Stock, Preference Stock and Preferential Stock, will be redeemed. None of PAWC's securities will be affected by the merger.

The transaction contemplated by the Merger Agreement required approval by the holders of AWWC voting stock. Accordingly, on December 5, 2001, following review by the Securities and Exchange Commission (SEC), AWWC issued a Proxy Statement describing the proposed transaction and notifying the holders of its voting stock of their right to vote in person or by proxy at the special meeting of stockholders scheduled for January 17, 2002. The stockholders' meeting was held as scheduled, and AWWC's shareholders approved the merger by a substantial margin. By letter dated

January 25, 2002, PAWC notified the Commission of the results of AWWC's shareholder vote.

B. Legal Requirements Regarding Mergers

As a preliminary matter before discussing the Exceptions, we note that any issue or Exception that we do not specifically address has been duly considered and will be denied without further discussion. It is well settled that we are not required to consider, expressly or at length, each contention or argument raised by the parties. *Consolidated Rail Corporation v. Pennsylvania Public Utility Commission*, 625 A.2d 741 (Pa. Cmwlth. 1993); also *see*, generally, *University of Pennsylvania v. Pennsylvania Public Utility Commission*, 485 A.2d 1217 (Pa. Cmwlth. 1984).

Also, before discussing the Exceptions, we will review the requirements of law regarding the burden of proof in this proceeding. As the proponent of a rule or order of this Commission, the Joint Applicants bear the burden of proof. 66 Pa. C.S. §332(a). The Pennsylvania Supreme Court has held that the term "burden of proof" means a duty to establish a fact by a preponderance of the evidence. *Se-Ling Hosiery v. Margulies*, 364 Pa. 45, 70 A.2d 854 (1950). The term "preponderance of the evidence" means that one party has presented evidence which is more convincing, by even the smallest amount, than the evidence presented by the other side. If a party has satisfied its burden of proof, it must then be determined whether the opposing party has submitted evidence of "co-equal" value or weight to refute the first party's evidence. *Morrissey v. Commonwealth of Pennsylvania, Department of Highways*, 424 Pa. 87, 225 A.2d 895 (1986).

Furthermore, any order of this Commission granting an application, in whole or in part, must be based on substantial evidence. *Dutchland Tours, Inc. v.*

Pennsylvania Public Utility Commission, 337 A.2d 922, 925 (Pa. Cmwlth. 1975). The term “substantial evidence” has been defined by the Pennsylvania Courts as such relevant evidence as a reasonable mind might accept as adequate to support a conclusion. More is required than a mere trace of evidence or a suspicion of the existence of a fact sought to be established. *Murphy v. Department of Public Welfare, White Haven Center*, 480 A.2d 382, 386 (Pa. Cmwlth. 1994); *Erie Resistor Corporation v. Unemployment Compensation Board of Review*, 194 Pa. Super. 278, 166 A.2d 96, 97 (1961).

Regarding the requirements for obtaining a certificate of public convenience in Pennsylvania, the applicable law for the factual setting in this proceeding is found in both the statutes and case law of the Commonwealth of Pennsylvania. Sections 1102 and 1103 of the Public Utility Code (Code) provide, in pertinent part:

§1102. Enumeration of acts requiring certificate

(a) General rule.-Upon the application of any public utility and the approval of such application by the commission, evidenced by its certificate of public convenience first had and obtained, and upon compliance with existing laws, it shall be lawful:

...

(3) For any public utility or an affiliated interest of a public utility as defined in section 2101 (relating to definition of affiliated interest), except a common carrier by railroad subject to the Interstate Commerce Act, [footnote omitted] to acquire from, or to transfer to, any person or corporation, including a municipal corporation, by any method or device whatsoever, including the sale or transfer of stock and including a consolidation, merger, sale or lease, the title to, or the possession or use of, any tangible or intangible property used or useful in the public service. Such approval shall not be required if:

(i) the undepreciated book value of the property to be acquired or transferred does not exceed \$1,000;

(ii) the undepreciated book value of the property to be acquired or transferred does not exceed the lesser of:

(A) 2% of the undepreciated book value of all fixed assets of such public utility; or

(B) \$5,000 in the case of personalty or \$50,000 in the case of realty;

(iii) the property to be acquired is to be installed new as a part of or consumed in the operation of the used and useful property of such public utility; or

(iv) the property to be transferred by such public utility is obsolete, worn out or otherwise unserviceable. Subparagraphs (i) through (iv) shall not be applicable, and approval of the commission evidenced by a certificate of public convenience shall be required, if any such acquisition or transfer of property involves a transfer of patrons.

66 Pa. C.S. §1102.

§1103. Procedure to obtain certificates of public convenience

(a) **General rule.**—Every application for a certificate of public convenience shall be made to the commission in writing, be verified by oath or affirmation, and be in such form, and contain such information, as the commission may require by its regulations. A certificate of public convenience shall be granted by order of the commission, only if the commission shall find or determine that the granting of such certificate is necessary or proper for the service, accommodation, convenience, or safety of the public. The commission, in granting such certificate, may impose such conditions as it may deem to be just and reasonable. In every case, the commission shall make a finding or determination in writing, stating whether or not its approval is granted. Any holder of a certificate of public convenience, exercising the

authority conferred by such certificate, shall be deemed to have waived any and all objections to the terms and conditions of such certificate.

66 Pa. C.S. §1103.

Sections 1102 and 1103 were interpreted by the Pennsylvania Supreme Court in *City of York v. Pennsylvania Public Utility Commission*, 449 Pa. 136, 295 A.2d 825 (1972), and provide the legal standard against which the question of approval of the Joint Application must be measured. In *City of York*, the Supreme Court said:

[A] certificate of public convenience approving a merger is not to be granted unless the Commission is able to find affirmatively that public benefit will result from the merger. . . . [T]hose seeking approval of a utility merger [are required to] demonstrate more than the mere absence of any adverse effect upon the public. . . . [T]he proponents of a merger [are required to] demonstrate that the merger will affirmatively promote the “service, accommodation, convenience, or safety of the public” in some substantial way.

City Of York, 449 Pa. at 141, 295 A.2d at 828.

C. Exceptions, Reply Exceptions, and Resolutions

1. Substantial Benefits from the Merger

The first issue raised on Exceptions which we will discuss is the issue of substantial benefits from the merger. The ALJ determined that the Joint Applicants presented sufficient evidence to meet the requirements delineated in *City of York, supra*. Accordingly, the ALJ recommended that the Application be approved subject only to the conditions to which the Joint Applicants have agreed. (I.D., pp. 24-27).

In their separately filed Exceptions, the OCA, the OTS, and the PennFuture Parties except to this recommendation. The OCA contends, among other things, that the ALJ failed to ensure that affirmative benefits will flow through to ratepayers and misapplied the standards in *City of York* in concluding that no further conditions beyond those accepted by the Applicants need be imposed. (OCA Exc., pp. 3-10). The OTS argues, among other things, that the ALJ erred in concluding that the quantification of benefits was not necessary and misapplied the *City of York* standards. (OTS Exc., pp. 3-13). The PennFuture Parties submit that the ALJ erred in reducing the Commission's role in ensuring substantial benefits flow to ratepayers by refusing to recommend conditions to which the Applicants have not agreed. (PennFuture Exc., pp. 5-7).

In their Replies to Exceptions, the Joint Applicants assert that the ALJ properly weighed the evidence and correctly applied the *City of York* standard, and that no quantification of benefits was necessary. (Applicants R.Exc., pp. 4-15).

In our consideration of these matters, we note the following. The OTS' own witness, Eric Van Jeschke, acknowledged, under cross-examination, that the positive attributes of the proposed merger identified by the Joint Applicants would, if realized, constitute affirmative public benefits (Tr., pp. 260-263). The OTS re-interprets *City of York* as requiring a dollar-and-cents "quantification" of such benefits before the Commission may approve a merger, acquisition, or change in control. In so doing, the OTS ignores the fact that this very same argument was rejected in the *City of York* case itself, as well as in subsequent Commission decisions.

The OTS relies on the Commission’s Opinion and Order approving the GPU/First Energy merger² as support for its “quantification” mandate. However, *GPU/FirstEnergy* can be distinguished from this proceeding in many respects. Most notably, GPU bundled its application for merger approval with a request to recover over \$300 million in purchased electric power costs by GPU’s subsidiaries’, Metropolitan Edison Company (MetEd) and Pennsylvania Electric Company (Penelec).³ Nevertheless, neither *GPU/FirstEnergy* nor the Commonwealth Court’s opinion affirming the Commission’s merger approval in that case⁴ made the “quantification” of public benefits an element of the *City of York* test.

The alleged need for a quantification of potential benefits or detriments was litigated by the protesting parties in *City of York*. In that proceeding, the Commission denied the protestants’ discovery requests that were designed and intended to “quantify” the rate effects of the proposed merger. *City of York, et al. v. York Telephone and Telegraph Company*, 45 Pa. P.U.C. 106 (1970). Notwithstanding the absence of quantification, the Pennsylvania Supreme Court had no difficulty affirming this Commission's decision to approve the merger and stated that the Commission's consideration of the “probable general effect of the merger upon rates” was all that the Code required. 295 A.2d at 829.

The OTS' argument that the *City of York* test cannot be met without quantifying the specific effects of alleged savings was also rejected by the Commission in

² *Joint Application for Approval of The Merger of GPU, Inc. With FirstEnergy Corp.*, Docket Nos. A-110300 F0095 and A-110400F0040 (Order entered June 20, 2001) (hereafter, *GPU/FirstEnergy*).

³ *Petition of Metropolitan Edison Company and Pennsylvania Electric Company for Interim Relief*, Docket Nos. P-00001860 and P-00001861 (Order entered June 20, 2001).

Application of Newtown Artesian Water Company and Indian Rock Water Company, 76 Pa. P.U.C. 260 (1992). The Commission accepted the Administrative Law Judge’s findings in that case as fully consistent with the *City of York*. The ALJ found that the proposed merger would produce lower financing costs over a prospective 25-year time period. 76 Pa. P.U.C. at 268.

Furthermore, in every major water utility merger or acquisition since *Newtown Artesian*, this Commission has relied upon findings that the transaction would likely produce lower capital costs or reduce other expenses without demanding that either the level of such savings or their impact on rates be quantified. *See, e.g., Application of United Water of Pennsylvania, Inc.*, Docket Nos. A-210013F0014 and A-230077F0003 (Order entered January 27, 2000) (*United*). In that proceeding, we determined that the transfer of control of a majority of UWR’s stock appeared to offer the possibility of greater amounts of capital being available as acquisition opportunities presented themselves in Pennsylvania.

In *GPU/FirstEnergy* (p. 38) and *ARIPPA* (792 A.2d at 656), this Commission approved a proposed merger and the Commonwealth Court affirmed that decision despite the absence of a “quantification” of “merger savings.” The Commonwealth Court found that it was lawful and appropriate to determine the amount of “merger savings” and the “disposition” thereof in a post-merger proceeding held to adjudicate rate-related issues raised by the MetEd/Penelec Petition for Interim Relief.

The quantification of merger savings was an issue in *GPU/FirstEnergy* only because of the unique facts of that case. As previously noted, the *GPU/FirstEnergy* application for merger approval was coupled with MetEd’s and Penelec’s “single issue”

⁴ *ARIPPA v. Pennsylvania Public Utility Commission*, 792 A.2d 636 (Pa.

rate filing to recover, or defer for future recovery, over \$300 million per year in purchased power costs the companies estimated they would incur to meet their Provider of Last Resort obligations. Other parties contended, and the Commission ultimately agreed, that it would not be proper or equitable to allow the utilities to recover \$300 million per year in additional costs at the same time GPU and its merger partner retained all of the anticipated “merger savings.” Because of the “rate caps” in place for MetEd’s and Penelec’s regulated electric distribution service, it was understood that neither company would be coming before the Commission in a base rate proceeding for several years, thereby eliminating the possibility that merger-related savings might be reflected in customers’ base rates any time soon.⁵

In contrast to *GPU/FirstEnergy*, a viable mechanism already exists for promptly reflecting any savings that may materialize from the proposed merger in PAWC’s rates. Unlike many of Pennsylvania’s regulated electric utilities, PAWC must seek rate relief on a regular basis because of the substantial capital investment which is necessary to meet new and evolving water quality standards and to replace aging infrastructure (*See* Joint Applicants’ Initial Brief, pp. 30-33). And, unlike *GPU/FirstEnergy*, the Joint Applicants agreed “up front” to pass back all savings that might be generated by the proposed transaction in PAWC’s future rate cases, while also agreeing to forego recovery of the acquisition premium, transaction costs and the retention bonuses created to ensure that key employees stay on after the transaction is consummated (Joint Applicants’ St. 1, p. 9; Joint Applicants’ St. 2, p. 8; I.D., p. 13).⁶ The normal process of

Cmwlth. 2002) (*ARIPPA*).

⁵ Apparently, a base rate filing would have been unlikely in any event, because evidence was adduced that MetEd’s and Penelec’s transmission and distribution service was producing a fair return. *See GPU/FirstEnergy*, p. 36; *ARIPPA*, 792 A.2d at 656.

⁶ GPU and First Energy acknowledged that “merger savings” could be used to reduce cost of service in a future transmission/distribution rate case, but only to the

examining and setting PAWC's base rates will capture any savings that might flow from the combination of American and Thames Holdings and will do so more promptly, accurately and thoroughly than the post-merger "quantification" approved in *ARIPPA*, *supra*.

For these reasons, we conclude that the ALJ properly applied the *City of York* standards in reaching his determination that the Applicants had met their burden of proof without a dollars-and-cents quantification of the public benefits. Neither the *City of York* nor any subsequent Commission Decision requires a dollars-and-cents quantification of public benefits. As noted above, and by the ALJ (I.D., pp. 24-26), the *City Of York* standard requires that the Joint Applicants demonstrate that the merger will affirmatively promote the convenience, safety, accommodation, or service of the public in some substantial way. To meet their burden of proof regarding the substantial merger benefits, the Joint Applicants presented credible evidence that the contemplated transaction will affirmatively promote the service, accommodation, convenience, or safety of the public.

Combining the largest investor-owned water company in the United States, PAWC's parent, with a member of the corporate family of the third largest water supplier in the world, RWE, will produce enhanced financing capabilities for the regulated utility, PAWC. By making AWWC part of a much larger and financially stronger company, the proposed transaction will substantially increase AWWC's access to capital at favorable rates. Currently, financing for the AWWC system is done on a consolidated basis through AWWC's financing subsidiary, American Water Capital Corporation (AWCC) (Joint Applicants' St. 4-R, p. 11). Prior to the announcement of the proposed transaction, AWCC's debt was rated A- and Baa1 by Standard and Poors and Moody's, respectively (Joint Applicants' St. 3-R, p. 5). In contrast, RWE is rated AA- by Standard and Poors

extent that such savings exceeded merger-related transaction costs. *See GPU/First*

and A1 by Moody's, which are both higher than AWCC's ratings (Joint Applicants' St. 3-R, pp. 5-6; Joint Applicants' St. 4-R, p. 10). Significantly, the announcement of the proposed transaction prompted the credit rating agencies to consider raising the AWWC/AWCC credit ratings to equal those of RWE (Joint Applicants' St. 4-R, p. 10). An upgrade in credit ratings translates into lower borrowing costs and, ultimately, savings for customers.

Additionally, AWWC's association with RWE will provide access to European capital markets, which is not currently available (Joint Applicants' St. 2, p. 10). The ability to place debt in non-domestic markets can provide substantial benefits because there are many times when debt can be issued at lower cost outside the United States as a consequence of domestic interest rate or market conditions. This increased flexibility in obtaining access to sources of capital is a benefit to PAWC's customers, albeit one that cannot currently be quantified.

Another anticipated benefit of the transaction is found in the area of research and development. The combination of AWWC and Thames will have a particularly beneficial effect for their respective research and development efforts because each has a somewhat different focus. AWWC is an industry leader in the identification and deactivation of pathogenic organisms such as giardia and cryptosporidium. Thames, in turn, has an equally high reputation in the areas of alternative treatment technologies, such as desalination, and facility management, rehabilitation and repair. For example, Thames is at the cutting edge of technological development in burst pipe prediction and "trenchless" pipe repair and rehabilitation (Joint Applicants' St. 1, p. 7; Joint Applicants' St. 2, p. 14). Thames' experience in these areas will be invaluable in assisting PAWC to meet the demands of future infrastructure

rehabilitation while minimizing capital costs (Joint Applicants' St. 2, p. 14). Moreover, Thames' annual budget for research and development, which approximated \$13 million in 2001, is considerably larger than that of AWWC, denoting the additional capability of the much larger company to fund essential research. This Commission has expressly found that this type of benefit satisfies the standard set by *City Of York*. See *United*, p. 3.

Accordingly, the Exceptions of the Parties regarding the issue of substantial merger benefits are denied.

2. The OCA's Rejected Conditions

The ALJ recommended adoption of the OCA's proposed conditions with which the Applicants agreed, but rejection of those not agreed to, since the Applicants had met their burden of proof without any conditions. The rejected conditions included restrictions regarding management risks, financial risks, regulatory risks, and service quality risks. They also included a rate reduction and "stay out" provisions. (I.D., pp. 27-32).

The OCA excepts to the ALJ's recommendation, arguing that the ALJ misunderstood the purpose of the OCA's rejected conditions, including the OCA's proposed rate reduction and "stay-out" provisions. The OCA contended that these rejected conditions are necessary to ensure substantial benefits to the ratepayers and the public. Consequently, the OCA submits that all of these rejected conditions must be imposed for the proper protection of the public. (OCA Exc., pp. 11-28).

In response, the Joint Applicants contend that the ALJ did not misconstrue the purpose of the OCA's rejected conditions. Instead, the Applicants assert that the ALJ

properly considered the evidence of record and concluded that the Joint Applicants had met their burden of proving substantial benefits of the merger without the rejected OCA conditions. For these reasons, the Joint Applicants argue that the OCA's Exceptions regarding its rejected conditions should be denied. (Applicants R.Exc., pp. 15-19).

Regarding this issue, we agree with the ALJ that, under Section 1103(a) of the Code, *supra*, we are authorized to impose any conditions and terms we deem to be "just and reasonable." We will separately address the OCA's proposed Condition Number 16, relating to the appropriate currency to be used in documents filed by PAWC with this Commission, below. However, we agree with the ALJ that the balance of the OCA's rejected conditions are neither necessary nor appropriate.

In discussing these conditions, we initially note that the Joint Applicants have agreed to eight significant conditions to the proposed merger. The Joint Applicants have agreed to forego any claim in future rate proceedings for the acquisition premium, transaction costs, and retention bonuses designed to retain key employees and officers. The Joint Applicants have also agreed to promptly report any downgrading of the bonds of RWE, Thames, AWWC or AWWC's subsidiaries. In addition, the Joint Applicants have agreed to maintain and provide access to English language versions of RWE's and Thames' annual reports, provide English language versions of documents produced in proceedings before this Commission, and maintain PAWC's books and records at a location within the United States. Importantly, the Joint Applicants have expressly agreed to safeguard the condition of PAWC's watershed land holdings. (Joint Applicants R.Exc., pp. 17, 18).

In its Exceptions, the OCA noted that a specific number of its proposed conditions had been rejected by the ALJ. (*See* OCA Exc., pp. 11-21). According to the

OCA: “The purpose of the conditions is to protect customers from the risks identified so that the transaction does not harm customers. If the conditions are not adopted by the PUC, then customers will be worse off than they are today.” *Id.*, p. 11.

The ALJ has recommended a finding that the Joint Applicants have satisfied their burden of proof in showing that the merger will provide a substantial public benefit. That is a sound recommendation and in full accord with all of the evidence of record. The fears and concerns raised by the OCA as justification for its proposed conditions are not born out by that same record. Excluding the OCA’s proposed Condition Number 16, the Joint Applicants have thoroughly rebutted each of the OCA’s contentions regarding the specific conditions rejected by the ALJ. (Joint Applicants’ R.Exc., pp. 11-18). As noted by the Joint Applicants, the OCA’s concerns rest largely on speculation or result in a demand for conditions that go farther than anything previously imposed by this Commission.

We find that the OCA’s proposed Condition Number 16 requires a different result. That Condition reads as follows:

Condition 16. Require that whenever PAWC is requested to provide documents to the Commission, or in any proceeding before the Commission, concerning the operations of RWE or any other subsidiaries or holdings of RWE, that all financial statements be provided in their original currency and in U.S. dollars (converted as of the date of the financial statement). For example, RWE’s financial statements as of December 31, 2001, would be provided in U.S. Dollars using

the conversion rate between dollars and euros on
December 31, 2001.

(OCA Exc., p. 23).

In its Exceptions, the OCA argues that its proposed Condition Number 16 “is a straightforward condition designed to ease the review and use of any financial statements. Further, it is essentially the companion condition to Condition 15, requiring that documents be provided in English.” (OCA Exc., p. 24). The Joint Applicants did not expressly respond to the OCA’s arguments on this Condition in their Reply Exceptions. However, in their Main Brief, the Joint Applicants argued that “Condition 16 . . . is . . . objectionable in that strict compliance could encompass a tremendous amount of work depending on the document(s) in question. Rather than having the Commission lay down a blanket rule, the Joint Applicants believe that this concern (i.e. currency conversion) can be best handled on a case-by-case basis.” (Joint Applicants’ M.B., p. 51).

We find that the OCA’s proposed Condition Number 16 is just and reasonable. As noted by the Joint Applicants, conversion of financial documents from euros to dollars can encompass “a tremendous amount of work.” However, this is work that should be performed by the corporation that is engaged in international business and not by Commission staff or other parties. Likewise, conversion of financial data is a cost of doing business that should be borne by the international corporation and not by the regulated company or its ratepayers. Good business practice seems to dictate that records be maintained in the currencies of all countries in which the corporation is doing business.

As a practical matter, the OCA’s proposed Condition Number 16 is necessary and appropriate. If requests for conversion of financial data were addressed on

a case-by-case basis, substantial delays in Commission proceedings could result. Moreover, case-by-case requests would be a significant and unnecessary drain on the resources of the Commission and other parties.

We will clarify the OCA's proposed Condition Number 16 in two respects. First, in accomplishing the currency conversion called for by that Condition, we shall require that the Financial Accounting Standards Board foreign currency translation pronouncements be applied. Second, we shall provide that if the original document is not in U.S. currency, then PAWC must certify the accuracy of the conversion. This second modification is consistent with the certification requirement in Condition Number 15 relating to translation of documents.

For the foregoing reasons, we will grant this Exception to the extent that the OCA's proposed Condition Number 16 is adopted. The balance of the OCA's Exception Number 2 will be denied.

3. The Environmental Protection Amendment and Water Shed Protection

The ALJ recommended rejecting the PennFuture Parties' argument that the Commission is under an affirmative duty in this proceeding to conserve and maintain the environment by virtue of the provisions of the Environmental Rights Amendment to the Pennsylvania Constitution (Article 1, §27). Article 1, §27 states:

§27. Natural resources and the public estate.

The people have a right to clean air, pure water, and to the preservation of the natural, scenic, historic and esthetic values of the environment. Pennsylvania's public natural resources are the common property of all the people, including generations yet to come. As trustee [*342] of these resources, the Commonwealth shall conserve and maintain them for the benefit of all the people.

The ALJ concluded that the Commission has a duty to protect the environment with respect to regulated public utilities. But the ALJ also determined that that oversight does not extend to future actions which might be taken by a third party. The ALJ also recommended rejecting the PennFuture Parties' conditions regarding 500 foot buffer strips around reservoirs and \$10 million funding for land trusts and conservatories. (I.D., pp. 34-36).

In their Exceptions, the PennFuture Parties contend, among other things, that the ALJ improperly avoided application of the Environmental Rights Amendment and provided insufficient protections for reservoirs and water supplies. (PennFuture Exc., pp. 7-11).

In their Replies to the Exceptions, the Joint Applicants argue that the ALJ properly rejected the PennFuture Parties' arguments regarding the Environmental Rights Amendment. The Joint Applicants maintain that, in the 30-year span since the adoption of that Amendment, neither this Commission nor any court has applied it in the manner that the PennFuture Parties propose. (Joint Applicants R.Exc., 19-21).

With respect to the Environmental Rights Amendment, we concur with the ALJ that the PennFuture Parties are incorrect in attributing to this Commission

affirmative duties to maintain the environment by virtue of the provisions of the Environmental Rights Amendment. In *Borough of Moosic v. Pennsylvania Public Utility Commission*, 429 A.2d 1237(1981), the Commonwealth Court said:

We view Section 27 to be self-executing only as it applies to the commission's regulation of a utility's *own* conduct which is within the ambit of the regulatory jurisdiction of the commission as created by statute and directly affects the environment.

429 A.2d at 1240 (emphasis in original). Thus, while this Commission has a duty to protect the environment under the Environmental Rights Amendment, our jurisdiction does not extend to future actions which a third party might take, even when those actions may be harmful to the environment. Other entities, including the Pennsylvania Department of Environmental Protection and county and local governments have jurisdiction to prevent or punish those harms.

Regarding the 500 foot buffer strips around PAWC reservoirs and the \$10 million funding for land trusts, we also concur with the ALJ that this Commission cannot, by the imposition of conditions, require actions beyond its jurisdiction in regulating public utility companies. *Cf. West Penn Railways v. Pennsylvania Public Utility Commission*, 135 Pa. Super. 89, 4 A.2d 545 (1939). For these reasons, we will deny the PennFuture Parties' Exceptions regarding the Environmental Rights Amendments, the 500 foot buffer strips, and the \$10 million funding for land trusts and conservancies.

Conclusion

We have reviewed the record as developed in this proceeding including the ALJ's Initial Decision and the Exceptions and Replies filed thereto. Based on our review, we shall grant in part and deny in part the Exceptions of the OCA. The Exceptions of the OTS and the PennFuture Parties will be denied; **THEREFORE,**

IT IS ORDERED:

1. That the Exceptions filed on July 11, 2002, by the Office of Consumer Advocate are granted, in part, and denied, in part, consistent with this Opinion and Order.

2. That the Exceptions filed on July 11, 2002 by the Office of Trial Staff and the Citizens for Pennsylvania's Future, d/b/a Penn Future, Defend Our Watershed!; Daniel S. Townsend, and Joseph Laver, to the Initial Decision of Administrative Law Judge Wayne L. Weismandel issued on June 21, 2002, are denied.

3. That the Initial Decision of Administrative Law Judge Wayne L. Weismandel is adopted, to the extent that it is consistent with this Opinion and Order.

4. That the written direct testimony of Eugene M. Brady filed by the Commission on Economic Opportunity on May 13, 2002, in the above-captioned case be stricken.

5. That the Protests filed by the Utility Workers Union of America, AFL-CIO and the Utility Workers Union of America Local Union No. 537 on January 11,

2002, by the Office of Consumer Advocate on January 14, 2002, and by Citizens for Pennsylvania's Future, d/b/a Penn Future, Defend Our Watershed!, Daniel S. Townsend, and Joseph Laver on March 1, 2002, in the above-captioned case are sustained in part and denied in part in accordance with the discussion contained in the Initial Decision.

6. That the Joint Application of Pennsylvania-American Water Company and Thames Water Aqua Holdings GmbH For All Approvals Required Under The Public Utility Code In Connection With A Change In Control Of Pennsylvania-American Water Company filed December 14, 2001, Docket Nos. A-212285F0096 and A-230073F0004, is granted, subject to the duly authorized officers of American Water Works Company, Inc., RWE Aktiengesellschaft, Apollo Acquisition Company, Pennsylvania-American Water Company, and Thames Water Aqua Holdings GmbH, having filed with the Pennsylvania Public Utility Commission within thirty (30) days of the entry date of the Commission's Order their fully-executed written acceptance of each of the following conditions:

a) Pennsylvania-American Water Company shall not include in its rates, in any fashion, any portion of the costs associated with the retention bonus program established pursuant to the Agreement and Plan of Merger dated September 16, 2001, between American Water Works Company, Inc., RWE Aktiengesellschaft, Thames Water Aqua Holdings GmbH, and Apollo Acquisition Company.

b) Pennsylvania-American Water Company shall not include in its rates, in any fashion, any portion of the acquisition premium or goodwill associated with the transaction occurring as a result of the Agreement and Plan of Merger dated September 16, 2001, between American Water Works Company, Inc., RWE

Aktiengesellschaft, Thames Water Aqua Holdings GmbH, and Apollo Acquisition Company.

c) Pennsylvania-American Water Company shall not include in its rates, in any fashion, any portion of the costs associated with analyzing, negotiating, consummating, or seeking approval of the transaction occurring as a result of the Agreement and Plan of Merger dated September 16, 2001, between American Water Works Company, Inc., RWE Aktiengesellschaft, Thames Water Aqua Holdings GmbH, and Apollo Acquisition Company.

d) Pennsylvania-American Water Company shall report to the Pennsylvania Public Utility Commission within thirty business days any downgrading of the bonds of RWE Aktiengesellschaft, Thames Water Aqua Holdings GmbH, American Water Works Company, Inc., or any subsidiary of American Water Works Company, Inc., including a full copy of the report issued by the bond rating agency.

e) Pennsylvania-American Water Company's Annual Report to the Pennsylvania Public Utility Commission shall include a complete, English-language copy of the annual reports of RWE Aktiengesellschaft and of Thames Water Aqua Holdings GmbH. This requirement can be satisfied by Pennsylvania-American Water Company's including in its Annual Report to the Pennsylvania Public Utility Commission an electronic reference or Internet link to an English-language copy of the annual reports of RWE Aktiengesellschaft and of Thames Water Aqua Holdings GmbH.

f) Whenever Pennsylvania-American Water Company is requested to provide documents to the Pennsylvania Public Utility Commission, or in any proceeding before the Pennsylvania Public Utility Commission, concerning the operations

of RWE Aktiengesellschaft or any other subsidiaries or holdings of RWE Aktiengesellschaft, those documents shall be provided in English. If the original document is not in English, then Pennsylvania-American Water Company must certify the accuracy of the English-language translation.

g) Whenever Pennsylvania-American Water Company is requested to provide documents to the Commission, or in any proceeding before the Commission, concerning the operations of RWE or any other subsidiaries or holdings of RWE, all financial statements shall be provided in their original currency and in U.S. dollars (converted in accordance with Financial Accounting Standards Board foreign currency translation pronouncements). If the original document is not in U.S. currency, then Pennsylvania-American Water Company must certify the accuracy of the conversion.

h) Pennsylvania-American Water Company shall keep its books and records at a location within the United States.

i) Pennsylvania-American Water Company shall continue to protect and safeguard the condition of all of its watershed land-holdings surrounding its reservoirs and well fields in Pennsylvania.

j) Pennsylvania-American Water Company shall maintain its existing watershed protection program arising out of the Commission-approved settlement in *Joint Application of Pennsylvania-American Water Company ("PAWC") and Pennsylvania Gas and Water Company ("PG&W") for approval of (1) the transfer, by sale, of substantially all of the water works property and rights of PG&W to PAWC including the subdivision of transferred real estate; (2) the commencement by PAWC of water service in the certificated territory of PG&W; and (3) the abandonment by PG&W*

of water service to the public, Docket Number A-212285F2002, Order adopted and entered December 14, 1995, as clarified by, Clarifying Order adopted and entered January 11, 1996.

7. That upon compliance with Ordering Paragraph No. 6, above, a certificate of public convenience be issued evidencing the Pennsylvania Public Utility Commission's approval of the transaction occurring as a result of the Agreement and Plan of Merger dated September 16, 2001, between American Water Works Company, Inc., RWE Aktiengesellschaft, Thames Water Aqua Holdings GmbH, and Apollo Acquisition Company, and the record at Docket Nos. A-212285F0096 and A-230073F0004 be then marked closed.

8. That upon non-compliance with Ordering Paragraph No. 6, above, the Joint Application of Pennsylvania-American Water Company and Thames Water Aqua Holdings GmbH for all approvals required under the Public Utility Code in connection with a change in control of Pennsylvania-American Water Company filed December 14, 2001, is dismissed, and the record at Docket Nos. A-212285F0096 and A-230073F0004 shall then be marked closed.

BY THE COMMISSION,

James J. McNulty
Secretary

(SEAL)

ORDER ADOPTED: August 29, 2002

ORDER ENTERED: September 4, 2002

BEFORE THE
COMMONWEALTH OF KENTUCKY
PUBLIC SERVICE COMMISSION

Application for Approval of the Transfer of Control of :
Kentucky-American Water Company to RWE AG and : Case No. 2002-00018
Thames Water Aqua Holdings GmbH :

Direct Testimony of
Scott J. Rubin

on Behalf of
Kentucky Office of Attorney General

April 26, 2002

Table of Contents

I. Introduction	1
II. Outline of Testimony	5
III. Management Risks	6
IV. Financial Risks.....	9
V. Regulatory Risks	25
VI. Service Quality Risks	28
VII. Summary of Conditions to Protect Consumers from Risks.....	30
VIII. Synergies from the Acquisition	34

1 **I. Introduction**

2 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

3 A. My name is Scott J. Rubin. My business address is 3 Lost Creek Drive, Selinsgrove, PA
4 17870.

5 Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

6 A. I am an independent attorney and consultant. My practice is limited to matters affecting
7 the public utility industry.

8 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS CASE?

9 A. I have been asked by the Office of Attorney General to review the proposed acquisition
10 of American Water Works Company, Inc. (AWW) by RWE AG (RWE), a multinational
11 corporation based in Essen, Germany. The transaction is structured as an acquisition by
12 Thames Water Aqua Holdings GmbH (Thames), a British corporation that is a wholly
13 owned subsidiary of RWE. My review includes the identification of potential risks and
14 benefits from the acquisition, with a particular focus on the risks and benefits to the
15 customers of AWW's Kentucky subsidiary, Kentucky-American Water Company
16 (KAWC).

17 Q. ARE YOU PERFORMING THIS REVIEW SOLELY FOR THE OFFICE OF ATTORNEY GENERAL?

18 A. No, I am not. While my testimony in this case is prepared solely for use in this
19 proceeding, I also have been retained by public advocates in New Jersey, Pennsylvania,
20 and West Virginia to conduct similar reviews in those jurisdictions. Similar testimony
21 was filed in the Pennsylvania proceeding on April 16, 2002.

22 Q. WHAT ARE YOUR QUALIFICATIONS TO PROVIDE THIS TESTIMONY IN THIS CASE?

1 A. I was employed by the Pennsylvania Office of Consumer Advocate (OCA) from 1983
2 through January 1994 in increasingly responsible positions. Since January 1994, I have
3 been an independent public utility consultant and attorney. I have developed substantial
4 expertise in matters relating to the economic regulation of public utilities. I have
5 published articles, contributed to books, written speeches, and delivered numerous
6 presentations, on both the national and state level, relating to regulatory issues. From
7 1990 until I left the OCA, I was one of two senior attorneys in that Office. Among my
8 other responsibilities in this position, I had a major role in setting the OCA's policy
9 positions on water and electric matters. In addition, I was responsible for supervising the
10 technical staff of that Office. I have testified as an expert witness before utility
11 commissions or courts in the District of Columbia and in the states of Arizona, Delaware,
12 Kentucky, Maine, New Jersey, New York, Ohio, Pennsylvania, and West Virginia. I
13 also have testified as an expert witness before the U.S. House of Representatives Science
14 Committee and the Pennsylvania House of Representatives Consumer Affairs
15 Committee. I also have served as a consultant to several national utility trade
16 associations and to state and local governments throughout the country. Appendix A to
17 this testimony is my curriculum vitae.

18 Q. WHAT IS YOUR UNDERSTANDING OF THE PROPOSED TRANSACTION BETWEEN AWW AND
19 RWE?

20 A. RWE, through its subsidiary Thames, is acquiring all of the common stock of AWW at
21 the price of \$46.00 per share payable in cash. At year-end 2001, AWW had
22 approximately 100 million shares of common stock outstanding, resulting in a purchase
23 price of approximately \$4.6 billion. In addition, RWE will be assuming the outstanding

1 debt of AWW, which is estimated to be approximately \$3.0 billion by the time of closing
2 (currently projected to be during the first half of 2003).

3 The acquisition will be made by Thames using funds supplied to it by RWE.
4 RWE anticipates funding the entire \$4.6 billion purchase price through the issuance of
5 bonds in U.S. dollars. Upon conclusion of the acquisition, AWW will be a subsidiary
6 either of Thames or of a new subsidiary created by Thames.

7 Q. WHAT DOCUMENTS HAVE YOU REVIEWED IN PREPARING YOUR TESTIMONY?

8 A. I have reviewed the application and supporting testimony of the applicants, as well as
9 documents provided by the applicants during discovery. I also have reviewed
10 applications, testimony, and discovery responses filed by other AWW subsidiaries and
11 Thames before other state utility commissions. In addition, I have reviewed all
12 documents filed by AWW with the Securities and Exchange Commission (S.E.C.)
13 concerning the transaction, as well as the annual reports for AWW and RWE for 2000
14 and 2001 (AWW's 2001 annual report is not yet available, but I have reviewed the Form
15 10-K that it filed with the S.E.C. on March 28, 2002) and various other S.E.C. filings of
16 AWW during the past two or three years. I also reviewed various presentations and
17 reports of RWE and Thames, including financial reports of RWE subsidiaries,
18 presentations to securities analysts in Europe, and similar documents available from
19 RWE's Internet site. Finally, I have attempted to follow news reports and analyses
20 concerning AWW, RWE, and Thames in the popular, trade, and financial media.

21 Q. ARE SOME OF THESE DOCUMENTS SUBJECT TO PROTECTION AS CONFIDENTIAL
22 INFORMATION?

1 A. Yes, on April 12, 2002 (modified on April 16, 2002), the Commission issued an order
2 finding that certain information provided by the applicants is exempt from public
3 disclosure. That order also protects, until approximately May 6, 2002 (to allow time for
4 the applicants to file an appeal), certain other information that the Commission found was
5 not confidential but for which the applicants had asserted a claim of confidentiality.
6 When I refer to information that the Commission has found to be confidential, I will mark
7 it by enclosing it in brackets and using a double underline like this **{begin confidential**
8 example **end confidential}**. When I refer to information that is protected until the appeal
9 period ends, I will clearly mark it by enclosing it in brackets without an underline, like
10 this **{begin protected example end protected}**.

1 **II. Outline of Testimony**

2 Q. HOW IS YOUR TESTIMONY ORGANIZED?

3 A. My testimony begins, in Sections III through VI, with a discussion of various categories
4 of risk associated with the proposed acquisition. In these sections, I am referring to risks
5 to the customers of KAWC as a result of the change in ownership and control of
6 KAWC's parent company. These risks include risks from change in management, risks
7 from RWE's need to finance (and ultimately pay for) the acquisition, risks of changes in
8 the regulatory jurisdiction of the Commission as a result of the transaction, and risks to
9 the quality of service received by KAWC's customers.

10 In Section VII, I summarize the conditions that the Commission should impose on
11 the acquisition in order to alleviate, or at least minimize, the risks that I identify. Without
12 these conditions, my conclusion is that the risks to consumers from the transaction are
13 substantial and will constitute a substantial detriment to KAWC's customers and the
14 Commonwealth as a whole. These conditions, then, are necessary to neutralize the
15 potential detriment from the acquisition; they do not provide consumers or the public
16 with any benefit vis-à-vis their current position.

17 Section VIII of the testimony discusses the synergies and other savings that
18 should be created by the acquisition. Also included in this section is a recommendation
19 for allocating those savings to KAWC's consumers. The allocation of savings to
20 consumers is necessary as a matter of fairness and as a way to provide further mitigation
21 of the risks posed by the transaction.

1 **III. Management Risks**

2 Q. WILL THE PROPOSED ACQUISITION OF AWW RESULT IN A CHANGE IN KEY MANAGEMENT
3 PERSONNEL?

4 A. There is always a possibility that the new owners will decide to make management
5 changes, or that existing officers and managers will decide that they do not want to work
6 for the new owners. In this case, AWW is taking steps to try to entice their existing
7 officers and managers to remain with the company, at least through the closing of the
8 transaction. AWW has established a \$15 million pool for the payment of “retention
9 bonuses.” These bonuses represent a multiple of an employee’s annual salary (the
10 bonuses range from 75% to 200% of the employee’s annual salary, depending on the
11 employee). Seventy-five percent of the bonus is payable on the date when RWE
12 purchases AWW, with the remaining 25 percent payable six months after closing.
13 (Definitive Proxy Statement, Dec. 5, 2001, pp. 29-30)

14 Q. WILL ANY EMPLOYEES OF KAWC, OR THE OTHER AWW SUBSIDIARIES THAT PROVIDE
15 SERVICES TO KAWC, RECEIVE THESE RETENTION BONUSES?

16 A. I don’t know. The applicants were asked for a list of employees who were offered these
17 bonuses, but the information was not provided. (AG 1-90, AG 2-19, LFUCG 1-31, Staff
18 2-3)

19 Q. SHOULD ANY OF THE RETENTION BONUS PAYMENTS BE INCLUDED IN KAWC’S COST OF
20 SERVICE?

21 A. Absolutely not. These payments should be borne solely by AWW and its shareholders,
22 and should not be passed through to the operating utilities either directly or indirectly.

1 These are costs associated solely with the proposed sale of the company to RWE; they
2 would not be necessary but for this transaction and they are not a routine part of
3 providing safe and reliable service to consumers.

4 Q. HAS THE COMPANY INDICATED WHETHER IT WILL CHARGE THESE COSTS TO CONSUMERS?

5 A. The company has stated that it will not attempt to charge these costs, either directly or
6 indirectly, to consumers (AG 1-79, AG 1-90, AG 1-91). These responses also state that
7 the costs will not be borne by the subsidiaries at all, but will be paid by the parent
8 company (AWW).

9 Q. WHAT DO YOU RECOMMEND?

10 A. I recommend that the Commission explicitly condition its approval of the acquisition as
11 follows:

12 Condition 1. Prohibit KAWC from including in its rates, in any fashion, any
13 portion of the costs associated with the retention bonus program.

14 Q. ARE RETENTION BONUSES SUFFICIENT TO ENSURE THAT KEY OFFICERS AND MANAGERS
15 WILL REMAIN WITH KAWC?

16 A. No, they are not. A retention bonus program is designed to keep key personnel in the
17 company until the acquisition and for a short period of time (six months, in this instance)
18 thereafter. After that, there is no certainty that key people will remain with the company.

19 Q. WHY SHOULD CONSUMERS OR THE COMMISSION CARE IF KEY EMPLOYEES REMAIN WITH
20 KAWC?

21 A. Consumers and regulators usually should not be concerned if there is a routine change in
22 management; however, wholesale changes in management can lead to periods of

1 inaction, loss of focus, and even a failure of the company to meet its responsibilities. For
2 example, losing one manager through a planned retirement usually is not a problem.
3 Losing ten managers in a period of a few weeks could pose serious problems.

4 Q. WHAT DO YOU RECOMMEND?

5 A. I recommend that the Commission condition its approval of the acquisition to impose a
6 reporting requirement on KAWC. Specifically:

7 Condition 2. Require KAWC to notify the Commission and intervenors
8 within five business days if any of its officers, managers, or key employees
9 leaves the employ of the company. (I would define “key employee” as
10 anyone who received a retention bonus payment.) The notification should
11 include an explanation of the reasons why the employee is leaving the
12 company and the plans for replacing the employee. I recommend that this
13 requirement remain in place for two years after the acquisition is closed. I
14 also would extend this notification requirement to officers of AWW and to
15 officers, managers, and key employees of those AWW subsidiaries that supply
16 essential services to KAWC, which are American Water Works Service Co.;
17 American Water Capital Corp.; and American Water Resources, Inc. (copies
18 of the agreements between KAWC and these affiliates were provided in AG
19 1-133).

20 Q. WHAT WILL THIS REPORTING REQUIREMENT ACCOMPLISH?

21 A. The reporting requirement will provide the Commission and parties with information that
22 might be used to investigate potential problems within the company or, perhaps, to
23 identify the need for a management audit or other study of KAWC’s operations to ensure
24 that it continues to meet its obligations to customers and the public.

1 **IV. Financial Risks**

2 Q. IS RWE PAYING A PREMIUM ABOVE BOOK VALUE FOR AWW?

3 A. Yes, it is. RWE estimates the purchase price of \$4.6 billion for AWW's common equity
4 represents a premium above book value of approximately \$2.8 billion (AG 1-108). In
5 other words, RWE is paying approximately 2.6 times book value for AWW's common
6 stock.

7 Q. DOES THIS CREATE ANY CONCERNS FOR KAWC'S CUSTOMERS?

8 A. Yes, it does. Whenever a utility is purchased for substantially more than book value,
9 concerns are raised about how the purchaser will achieve a reasonable return on its
10 investment, thereby ensuring its financial health. This is particularly a concern with
11 AWW where nearly all of its business is regulated.

12 Q. BEFORE YOU GO ANY FURTHER, HOW DO YOU KNOW THAT NEARLY ALL OF AWW'S
13 BUSINESS IS REGULATED?

14 A. AWW's Form 10-K, dated March 28, 2002, divides the company into two "segments" for
15 reporting purposes: regulated and unregulated. During 2001, the regulated segment
16 accounted for more than 95 percent of the revenue from external sources (\$1,377 million
17 out of a total of \$1,439 million); all of the net income (\$196.1 million out of a total of
18 \$193.4 million); and 95 percent of the assets (\$6,317 million out of a total of \$6,630
19 million) (these figures exclude the "other" category shown in AWW's report).

20 Q. CAN YOU ILLUSTRATE THE PROBLEM OF A UTILITY BEING PURCHASED FOR SUBSTANTIALLY
21 MORE THAN BOOK VALUE?

1 A. Yes, I will give a simple example. Let us assume that a utility has a book value of \$1,000
2 and that its overall cost of capital is 10 percent. That means that its investors anticipate
3 receiving a return of \$100 on the \$1,000 invested in the utility's rate base. But what
4 happens if another company buys this utility for \$2,600? If the utility's rates continue to
5 be set based on the historical cost, or book value, of the assets, then the utility will still
6 earn a return of \$100. This represents a return to the new investors of just 3.8 percent,
7 which is well below their cost of capital in this example. In order to earn a 10 percent
8 return on the purchase price, of course, the return would need to increase to \$260.

9 Q. ARE THERE OTHER WAYS THAT INVESTORS COULD EARN A REASONABLE RETURN ON THEIR
10 INVESTMENT?

11 A. Yes, I will list several ways that a purchaser could try to achieve a reasonable return on
12 its investment in a regulated utility where the purchase price greatly exceeds book value.

13 1. The purchaser could fund the purchase price with capital that is less costly than
14 the weighted cost of capital. If regulators do not reduce the authorized cost of capital to
15 reflect this fact, then the purchaser can achieve a return that more closely matches the
16 cost of capital that it invested in the purchase. For example, if the purchaser in my
17 example is able to borrow the entire purchase price at a 5 percent interest rate, then its
18 cost of capital would be $5\% \times \$2,600$, or \$130.

19 2. The new purchaser can find ways to make the utility more efficient. If it can
20 avoid recognizing all of those cost savings in rates, then it can come closer to receiving
21 its cost of capital. Similarly, the new purchaser may decide to defer maintenance or
22 otherwise reduce expenditures in an attempt to come closer to achieving its desired
23 return.